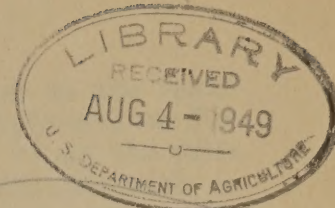


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UNITED STATES DEPARTMENT OF AGRICULTURE
Rural Electrification Administration

LS-M1



June 14, 1944

Administrative Memorandum

SUBJECT: Basis for Determination of Self-liquidation of Proposed Loans

In General

The determination that loans made in accordance with Section 4 of the Rural Electrification Act are self-liquidating and will be repaid in whole or in part out of income within the loan period shall be made on the basis of a finding that during the period of the loans the consumption of electric energy at the rates to be charged will produce estimated revenues and receipts sufficient to cover: (1) all expenditures essential to the operation of the system, to maintaining and preserving the properties in good repair and working order, and to keeping the properties in continuous operation in order to furnish the consumers served with a dependable supply of electric energy; and (2) all payments in respect of principal of and interest on the Government loans when and as the same shall become due.

The studies on which such findings are based shall be made of the combined system as an integrated unit and not merely of each subsequent section that may be added from time to time and for which a proposed loan is under consideration; and each such system shall be considered on its individual merits. Inasmuch as the average applicant for rural electrification loans does not have a long established record as a business enterprise with a large investment of equity capital and a financial credit rating, the approach to the examination of applications must of necessity be considerably different from that resorted to by a conventional lending agency. Although there can be no definite list of specific requirements which every project must meet in order to be found self-liquidating, there are certain economic factors that are fundamental to a determination that a proposed loan will be self-liquidating. The following considerations are basic to such a finding.

Determination of Estimated Revenue and Receipts

The estimated revenue and receipts shall be calculated on the basis of the estimated number of consumers that will be served, the estimated consumption per consumer per month, and the proposed schedule of retail rates. The

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estimated number of consumers to be served shall be determined on the basis of the certified tabulation of the persons who have signed applications for service and an estimate of the number of potential consumers along the proposed lines that did not sign applications but experience indicates will take service, after the lines are constructed. Frequently there are persons located along proposed lines who are reluctant to sign applications during the initial survey and want to wait until construction is under way or completed before they indicate they will take service. In reflection of this situation, provision shall be made in the estimate for such potential consumers and new types of enterprise. The actual percentage used in any particular instance shall be dependant primarily on the results of a field survey although generally on the basis of experience 50 per cent of the potential consumers is taken into consideration for the purpose of self-liquidation studies.

In determining the estimated average consumption per consumer, consideration shall be given to the experience of operating systems in areas of similar economic and productive characteristics; the application of electric power to productive use determined by the prevailing type of farming and other related enterprises existing in the area; effect of electric service toward the stimulation of new enterprises, and other economic activities in the community; the general progressiveness of the farm people and their willingness to adopt new methods and techniques with the use of electricity in farming operations; and the influence of low wholesale power rates available in the area and corresponding low retail rates, including the amount of the minimum bill.

Determination of Estimated Construction Costs

The estimated construction cost of the proposed project shall be determined on the basis of the estimated consumers, their estimated consumption, and the facilities required to serve them. Using these as a basis, an allotment budget shall be prepared to show in detail all factors entering into the cost of the project, including engineering, construction, legal services, insurance, supervision, rent, salaries, and overhead.

Determination of Estimated Operating Expenditures

The estimated operating expenditures of the proposed project shall be determined on the basis of expenditures that the borrower will have to make during the loan period to keep the properties in good repair and working order, and to pay the cost of salaries, insurance, taxes, power, rent, and other items of expense essential to providing continuous, dependable electric service to the consumers, and to make payments of interest and principal on the Government loans when and as they become due. For purposes of self-liquidation studies, the estimated expenditures of the borrower during the

life of the loan shall include an estimate of all normal operating expenses of the borrower to the extent that they result in the expenditure of funds by the borrower during such period. The estimated expenditures shall not include, however, any provision for additions of capital improvements or catastrophic replacements to the properties or keeping the total book value of the borrowers' assets equal to their original cost throughout the loan period. Provision for such items is a managerial decision for which the borrowers are primarily responsible.

Final Determination of Self-Liquidation of Proposed Loan

The final determination of whether a proposed loan is self-liquidating and will be repaid in whole or in part out of income during the period of the loan shall be based on a comparison of the estimated annual revenues with the estimated annual expenditures as shown by the above studies. A surplus of estimated revenues over the expenditures will constitute a basis for a finding that the loan would be self-liquidating and may be considered for final action.

/s/ WILLIAM J. NEAL

Acting Administrator

life of the loan shall include an estimate of all normal operating expenses of the borrower to the extent that they result in the expenditure of funds by the borrower during the period. The estimated expenditures shall not include, however, any expenditures for additions of capital improvements or extraordinary expenditures to the properties or keeping the total book value of the borrower's assets equal to their original cost throughout the loan period. Provision for such items is a managerial decision for which the borrower is primarily responsible.

Final Determination of Self-Liquidation of Borrowed Loan

The final determination of whether a borrowed loan is self-liquidating and will be repaid in whole or in part out of income during the period of the loan shall be based on a comparison of the estimated annual revenues with the estimated annual expenditures as shown by the above schedule. A surplus of estimated revenues over the expenditures will constitute a basis for stating that the loan would be self-liquidating and may be considered for final action.

(s) WILLIAM J. SHAW

Acting Administrator